INDEX

CITATIONS

Cases:

In the Supreme Court of the United States

October Term, 1945

No. 966

Herbert L. Stern, petitioner

v.

Carter H. Harrison, Collector of Internal Revenue

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 90–102) is reported at 55 F. Supp. 687. The opinion of the Circuit Court of Appeals (R. 126–131) is reported at 152 F. 2d 321.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on December 18, 1945. (R. 132.)

The petition for a writ of certiorari was filed on March 18, 1946. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether, as the lower court held, the gain realized by taxpayer on the redemption of his shares of preferred stock in Balaban & Katz Corporation, pursuant to a plan for complete redemption and cancellation of one half of the preferred stock of the corporation, was a distribution in "partial liquidation" as defined in Section 115 (i) of the Revenue Act of 1936 and hence taxable in its entirety under Section 115 (c) of the Act; or whether, as taxpayer contends, the gain was taxable as a capital gain upon the sale and exchange of a capital asset subject to the limitations contained in Section 117 (a) of the Revenue Act of 1936.

STATUTES AND OTHER AUTHORITIES INVOLVED

The applicable statutes and other authorities are printed in the Appendix, *infra*, pp. 24–28.

STATEMENT

The facts were stipulated (R. 23–86) and may be summarized as follows:

Balaban & Katz Corporation (hereinafter referred to as "B & K") was incorporated in 1923 under the laws of the State of Delaware. As of

December 29, 1934, its outstanding capitalization consisted of the following[1] (R. 25):

264,206 shares of common stock of a stated value of	$6,605,150
26,126 shares of 7% cumulative preferred stock par value $100 a share, redeemable at $110 plus accumulated dividends—par value	2,612,600
Serial 5½% gold notes in the principal amount of	2,924,500
Serial 6% gold notes in the principal amount of	128,000

At this time B & K had no substantial bank obligation. (R. 25.)

On May 1, 1935, all of the 5½% and 6% serial gold notes were retired with funds obtained from a bank loan of $2,400,000 bearing interest at 3¼%, plus current funds of B & K, including those held in reserve for serial retirement of the notes. (R. 25.)

Thereafter B & K negotiated with the same bank for an additional loan with a view toward replacing some or all of its outstanding 7% preferred stock with the proceeds of such loan which would bear interest at a rate less than the preferred dividend rate of 7%. (R. 25).

B & K's certificate of incorporation provided that the 7% preferred stock was subject to redemption at any time at $110 per share and all accrued dividends, or by corporate purchase at less than the redemption price. (R. 80.) The certificate also provided that (R. 80)—

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[1] B & K was authorized to issue 270,000 shares of common stock (par value $25 per share) and 28,700 shares of preferred stock. (R. 79.)

> Preferred stock retired, redeemed or purchased, as herein provided, shall not be reissued, and no preferred stock shall be issued in lieu thereof or in exchange therefor.

At a meeting of the Board of Directors of B & K held on February 5, 1936, a "plan for the redemption and retirement of the outstanding shares of preferred stock" was presented and adopted (R. 25, 28–29); and it was resolved to increase and consolidate the bank loans to an amount not in excess of $3,300,000 with interest not in excess of 3⅛% (R. 29); to give notice for redemption and retirement of one-half of the preferred stock, such redemption to be in accordance with the terms of the charter and by-laws; to withdraw the preferred stock from the list of the Chicago Stock Exchange; and to acquaint the preferred stockholders with the intention of the corporation to redeem and retire all of its preferred stock over a period of years, as set forth in the plan of redemption and retirement (R. 30).

Pursuant to this resolution the outstanding bank loan was increased by $1,373,500 to $3,300,000, bearing interest at 3⅛% (R. 26), the principal being payable within five years from the date thereof, May 1, 1936 (R. 58). In accordance with the plan for redemption and retirement of preferred shares, B & K gave "Notice of Redemption of Preferred Stock" on March 1, 1936, to the preferred stockholders, advising that one-half of

the holdings of each of record on April 3, 1936, would be called for redemption on May 1, 1936, in accordance with the certificate of incorporation, by the payment of $110 per share and accrued dividends. (R. 26, 64–67.) The form "Letter of Transmittal" recited that the preferred stockholder delivered his certificates to the corporation "for redemption" and requested that a check be issued "for the redemption price of the shares to be redeemed on May 1, 1936, and accrued and unpaid dividends thereon to May 1, 1936" and a certificate be issued to him for the number of shares deposited and "not redeemed on May 1, 1936"[2] (R. 68–69.)

Pursuant to this notice to preferred stockholders B & K acquired 12,995 shares of its outstanding preferred stock, leaving 13,061 shares outstanding. (R. 26.) At this time its earned surplus was in excess of $3,000,000. (R. 70, 71.)

On April 28, 1937, a "Certificate of Retirement of preferred stock of Balaban and Katz Corporation," dated February 16, 1937, was filed,

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[2] By corporate resolution the transfer agent was directed, in connection with the issuance of certificates evidencing that portion of preferred shares not redeemed, to stamp upon each certificate (R. 48):

"The Shares of Stock Evidenced by This Certificate Are Not Subject to Nor Entitled to the Benefit of the Redemption Effective and Applicable to One-Half (½) of the Preferred Stock of Balaban & Katz Corporation Which Was Outstanding on May 1, 1936."

as certified by the Secretary of State of Delaware, providing in part (R. 26–27)—

> First: That, pursuant to the provisions of Section 27 of the General Corporation Law of the State of Delaware, as amended, and subject to the provisions of its Certificate of Incorporation, the corporation has, by resolution of its board of directors, retired Thirteen Thousand Fifty-five (13,055) shares of its issued and outstanding Preferred Stock of the par value of One Hundred Dollars ($100.00) per share, heretofore purchased by it out of its surplus.
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> Second: That the capital of the corporation is hereby reduced by the amount of capital represented by the shares so purchased and retired, to-wit: One Million, Three Hundred Five Thousand, Five Hundred Dollars ($1,305,500.00).
>
> Third: That the Certificate of Incorporation of the corporation prohibits the reissue of said shares when so purchased and retired; and accordingly, pursuant to the provisions of said Section 27, upon the filing and recording of this certificate as therein provided, the Certificate of Incorporation of the corporation shall be amended so as to effect a reduction in the authorized Preferred Stock of the corporation to the extent of One Million, Three Hundred Five Thousand, Five Hundred Dollars ($1,305,000), being the aggregate par value of said Thirteen Thousand Fifty-

five (13,055) shares of such stock so purchased and retired.

Among the preferred shares redeemed by B & K in 1936 were 561 shares transferred by the taxpayer, which shares had a total cost to him for income tax purposes of $39,059.84 The taxpayer received from the corporation for this stock the amount of $61,710, yielding a profit to him of $22,650.16. (R. 24.) In his income tax return for 1936, taxpayer reported this amount as a capital gain realized upon the sale or exchange of a capital asset, but treated only $8,964.55 as includible in income under Section 117 (a) of the Revenue Act of 1936. (R. 24.) The Commissioner determined that the profit of $22,650.16 was taxable in its entirety as a distribution in partial liquidation under the provisions of Section 115 (c) and (i) of the Revenue Act of 1936, resulting in a deficiency in taxpayer's income tax for 1936 of $8,485.08. (R. 24.)

Taxpayer paid the deficiency, with interest thereon, on January 19, 1938, and on June 27, 1938, filed claim for refund of $8,485.08, plus interest of $342.40, total $8,856.57. On July 18, 1940, the Commissioner notified taxpayer of his disallowance of the claim for refund. The present suit was instituted on June 30, 1942. (R. 24.)

In its judgment order the District Court found the facts substantially as stipulated. (R. 102–

107.) However, it added the following to the stipulated facts (R. 107–108):

> The sale of Balaban & Katz Corporation preferred stock by plaintiff during 1936 here involved was one step in, and may not be dissociated from all of the other attendant circumstances and transactions which form a part of, an elaborate plan of refinancing or recapitalization adopted and put into effect by Balaban & Katz Corporation by eliminating notes and preferred stock which bore high rates of interest, and substituting therefor a bank loan or loans carrying a much lower rate of interest, thereby increasing the net income for the payment of dividends on the common stock; the corporate structure was in no wise changed, the total assets or total capitalization were not decreased, no steps taken toward liquidating the business in any way, the only result of the transaction being to increase the net income available for the payment of dividends on the common stock.
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> The position of Balaban & Katz Corporation as one of the leading motion picture exhibitors in the Chicago area was not changed as a result of the recapitalization plan which was put into effect during 1935 and 1936, nor were its assets, aggregate debt and stock capitalization, or operations reduced in any way by the adoption of the plan; the acquisition of preferred stock did not involve anything like a partial liquidation, nor was it in accordance with any

bona fide plan of liquidation within the ordinary meaning of that term; apart from any question of the income tax consequence of the effect upon a statutory provision of the motive or intent of taxpayer or any other person, the transaction here involved viewed in its entirety does not come within the meaning of the term "amounts distributed in partial liquidation of a corporation" as defined in Section 115 (i) of the Revenue Act of 1936; the ultimate goal sought to be accomplished by Balaban & Katz Corporation, without giving any consideration to the intent of the parties, was not in reality a partial liquidation of that corporation but rather amounted to an expansion of the same.

The District Court concluded as a matter of law that Section 115 (c) of the Revenue Act of 1936 does not apply to a transaction which is not in effect liquidating and as a result of which there is no diminution in the assets, capitalization or operations of the corporation's business and that Section 115 (i) of the Act does not include transactions which are not in effect liquidating; hence that the redemption of its preferred stock by B & K in 1936 did not amount to a distribution in partial liquidation. (R. 108.)

The Circuit Court of Appeals reversed. (R. 126–131.) It held that the stipulated facts show that in 1936 B & K decreased its outstanding preferred stock by one-half; accordingly, that the

District Court's finding that the corporate structure was not changed and that the total capitalization was not decreased was erroneous (R. 129–130); that the cancellation and redemption of half of all the preferred stock falls within the definition of amounts distributed in partial liquidation contained in Section 115 (i) of the Revenue Act of 1936, and that the gain thereon realized by the taxpayer is therefor taxable in its entirety under the provisions of Section 115 (c) of the Act. (R. 130.)

ARGUMENT

(1) Section 115 (i) of the Revenue Act of 1936 (Appendix, *infra*, p. 25) defines the term "amounts distributed in partial liquidation," as used in Section 115, as—

> a distribution by a corporation in complete cancellation or redemption of a part of its stock, or one of a series of distributions in complete cancellation or redemption of all or a portion of its stock.

There is no proof that the distribution in redemption of stock on May 1, 1936, was one of a series of distributions,[3] and consequently only the

[3] Although the directors adopted a resolution at their meeting on February 5, 1936, that the officers should give notice to preferred stockholders of the present intention of the corporation to redeem and retire over a period of years all of the preferred stock, as set foth in the plan (R. 30), the stipulation does not show that any further distributions in redemption of the stock were made, and the certificate filed

first part of the definition is pertinent here.

As the facts set out in the Statement, *supra,* show, B & K adopted a stock redemption plan, and pursuant thereto, called in all of its outstanding preferred stock certificates, issued a new certificate to each stockholder for one-half the number of shares represented by the old certificate, retired and cancelled the other half of the shares as of May 1, 1936, distributed the amount of $110 per share and the accrued dividends thereon in payment for the shares so retired and cancelled, and was forbidden by its charter to reissue retired, redeemed, or repurchased preferred stock. The corporation, therefore, made a distribution in complete cancellation or redemption of a part of its stock, i. e., one-half of its outstanding preferred stock. Thus, the redemption transaction fits exactly within the first definition of partial liquidation in Section 115 (i) and also within Article 115-5 of Treasury Regulations 94 (Appendix, infra, pp. 26-27), pro-

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with the Secretary of State of Delaware on April 28, 1937, states that 13,055 shares of the outstanding preferred stock (one-half) only have been retired (R. 26-27). This was the amount of stock to be redeemed in 1936 in accordance with the plan. The stipulation states that pursuant to the notice of redemption B & K acquired 12,995 shares. (R. 26.) The slight discrepancy of 60 shares between the shares stated in the certificate of retirement (13,055) as having been retired and the 12,995 shares acquired pursuant to notice of redemption is not explained, but in any case it is not inferable from this small inconsistency that there was a second distribution in cancellation or redemption of stock.

viding that a complete cancellation or redemption of a part of corporate stock may be accomplished, *inter alia,* by taking up all the old shares of a particular series and issuing new shares to replace a portion thereof, or by the complete retirement of any part of the stock, whether or not pro rata. See also *Kelly* v. *Commissioner,* 97 F. 2d 915 (C. C. A. 2d); *Malone* v. *Commissioner,* 128 F. 2d 967 (C. C. A. 5th).

As the Circuit Court of Appeals held (R. 130), the District Court's determination (R. 107–108) that the stock capitalization of B & K was not decreased and its capital structure was not changed is entirely unsupported and is contrary to the stipulated facts that one-half of the shares of preferred stock were retired and could not, under B & K's charter, be reissued, that the capital of the corporation was reduced by $1,305,500, and that the certificate of incorporation was amended to reflect these changes (R. 26–27). Indeed, the taxpayer makes no contention that one-half of the outstanding shares of preferred stock of B & K were not cancelled and redeemed completely but relies instead on the view of the District Court that a distribution in complete cancellation or redemption of a part of a corporation's stock is not a distribution in partial liquidation within the meaning of Section 115 (i), even though it complies literally with the statutory definition, unless it is accompanied by a re-

trenchment of corporate business or represents a distribution of idle corporate assets. (Pet. Br. 23–27.)

But the District Court's view of the statutory requirements was erroneous, as the Circuit Court of Appeals held. The statutory definition itself prescribes no such criteria as a curtailment or partial liquidation of corporate business. The question is not whether there was a partial liquidation in the usual or ordinary sense. 1 Mertens, Law of Federal Income Taxation, Sec. 9.83, pp. 547–548; *Salt Lake Hardware Co.* v. *Commissioner,* 27 B. T. A. 482; *Robinson* v. *Commissioner,* 42 B. T. A. 725, 735. As the Tax Court said in *Allport* v. *Commissioner,* 4 T. C. 401, 403, dismissed and affirmed January 29, 1946 (C. C. A. 7th)—

> The statute applies, not to a distribution in liquidation of the corporation or its *business,* but to a distribution in cancellation or redemption of a part of its *stock.*

Moreover, the settled construction has been that a distribution in complete cancellation or redemption of a part of corporate stock is a partial liquidation within Section 115 (i), irrespective of whether or not it is accompanied by an intent to curtail or liquidate the corporate business or any part thereof. See *Yankey* v. *Commissioner,* 151 F. 2d 650 (C. C. A. 10th); *Commissioner* v. *Quackenbos,* 78 F. 2d 156 (C. C. A. 2d); *Malone*

v. *Commissioner,* 128 F. 2d 967 (C. C. A. 5th); *Hill* v. *Commissioner,* 126 F. 2d 570 (C. C. A. 5th); *Alpers* v. *Commissioner,* 126 F. 2d 58 (C. C. A. 2d); *Amelia H. Cohen Trust* v. *Commissioner,* 121 F. 2d 689 (C. C. A. 3d); *Hammans* v. *Commissioner,* 121 F. 2d 4 (C. C. A. 2d); *Kelly* v. *Commissioner,* 97 F. 2d 915 (C. C. A. 2d); *Mittelman* v. *Commisisoner,* 5 T. C. 932, 939–940; *R. D. Merrill Co.* v. *Commissioner,* 4 T. C. 955; *Cochran* v. *Commissioner,* 4 T. C. 942, 951; *Allport* v. *Commissioner* 4 T. C. 401, 403, dismissed and affirmed January 29, 1946 (C. C. A. 7th); *Irvine* v. *Commissioner,* 46 B. T. A. 246; *Coley* v. *Commissioner,* 45 B. T. A. 405, appeal dismissed May 25, 1942 (C. C. A. 5th); *Robinson* v. *Commissioner,* 42 B. T. A. 725; *Britt* v. *Commissioner,* 40 B. T. A. 790, 795–796, affirmed on other grounds, 114 F. 2d 10 (C. C. A. 4th); *Salt Lake Hardware Co.* v. *Commissioner,* 27 B. T. A. 482; see also 1 Mertens, Law of Federal Income Taxation, Section 9.83.[4]

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[4] *Beretta* v. *Commissioner*, 141 F. 2d 452 (C. C. A. 5th), certiorari denied, 323 U. S. 720, alone contains language suggesting that an intention to liquidate the business is necessary to constitute a partial liquidation, as first defined in Section 115 (i), but since there was no complete cancellation or redemption of a part of the stock, but only a reduction in par value of all the stock in that case, there was no distribution in partial liquidation within the statutory definition in any event; hence the discussion regarding the necessity for a liquidating intent was *obiter* in that case.

(Footnote Continued on Page 15)

Section 115 (i) is not concerned with the reasons for, or the circumstances surrounding, a dis-

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Of course, an intention to liquidate the corporation is manifestly necessary, under that portion of the second definition of partial liquidation contained in Section 115 (i), to demonstrate that a distribution is one of a series of distributions in complete cancellation or redemption of all of the stock. See e. g., *Shellabarger Grain Products Co.* v. *Commissioner*, 146 F. 2d 177, 181 (C. C. A. 7th); *Rheinstrom* v. *Conner*, 125 F. 2d 790 (C. C. A. 6th), certiorari denied, 317 U. S. 654; *Tate* v. *Commissioner*, 97 F. 2d 658 (C. C. A. 8th), certiorari denied, 305 U. S. 639; *Holmby Corp.* v. *Commissioner*, 83 F. 2d 548 (C. C. A. 9th); *Canal-Commercial T. & S. Bk.* v. *Commissioner*, 63 F. 2d 619 (C. C. A. 5th), certiorari denied, 290 U. S. 628. Indeed, *Wilcox* v. *Commissioner*, 43 B. T. A. 931, affirmed, 137 F. 2d 136 (C. C. A. 9th), relied on by taxpayer (Br. 24), is a case in which it was held that a distribution was not one of a series in complete cancellation or redemption of all or a portion of stock, since there was only a reduction in par value of all the stock. The language quoted by taxpayer (Br. 24–25) from the Board's opinion was used in connection with the second definition of partial liquidation in Section 115 (i), which is not involved in the instant case. See, *supra*, pp. 10–11.

Furthermore, certain cases have made a distinction between acquisition by a corporation of its own stock for purposes of retirement, that is, complete cancellation or redemption, and acquisition to hold as treasury stock until reissued. Acquisitions of the latter type have been held not to be partial liquidations within Section 115 (i) on the theory that the corporation does not alter its capital structure by complete cancellation of stock. See, e. g., *Amelia H. Cohen Trust* v. *Commissioner*, 121 F. 2d 689 (C. C. A. 3d); *Fry* v. *Helvering*, 128 F. 2d 737 (C. C. A. 2d). This doctrine has even been extended to a case where the corporation could legally reissue the stock which it acquired and retired. *Alpers*

(Footnote Continued on Page 16)

tribution in complete cancellation or redemption of a part of the stock.[5] Consequently, it is immaterial that the cancellation and redemption of

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v. *Commissioner*, 126 F. 2d 58 (C. C. A. 2d). Upon such a question the presence or absence of a liquidating intent may be relevant. In its opinion (R. 95–96, 97–98) the District Court relied on cases (*Hadley* v. *Commissioner*, 1 T. C. 496; *Smith* v. *Commissioner*, 38 B. T. A. 317; *Berger* v. *Commissioner*, decided January 12, 1939 (1939 C. C. H. B. T. A. Memorandum Decisions Service, par. 10, 561–E), appeal dismissed, 106 F. 2d 999 (C. C. A. 6th)), involving corporate acquisitions of treasury stock, not acquisitions for retirement and cancellation, as here. This was so also in *Harter Bank & Trust Co.* v. *Gentsch*, 60 F. Supp. 400 (N. D. Ohio), and *Trust Co. of Georgia* v. *United States*, 60 F. Supp. 470 (C. Cls.), cited by taxpayer (Br. 25, 26). The quoted statements from these cases with respect to an intention to liquidate must be read in the light of the question there under consideration.

[5] These might be pertinent, of course, if the question were whether the distribution in complete cancellation or redemption of a part of corporate stock, otherwise within Section 115 (i) and (c), was made at such time and in such manner as to be essentially equivalent to the distribution of a taxable dividend, so that Section 115 (g) (Appendix, *infra*, p. 25) would require that the distribution be treated as a taxable dividend (to the extent that it represents a distribution of earnings or profits accumulated after February 28, 1913). Cf. *Flanagan* v. *Helvering*, 116 F. 2d 937 (App. D. C.), in which it was pointed out (p. 939) that proof as to whether the corporation is a going concern or is curtailing its activities is pertinent to the question whether the distribution is in essence a dividend. Cf. also *Smith* v. *United States*, 121 F. 2d 692 (C. C. A. 3d); *Hirsch* v. *Commissioner*, 124 F. 2d 24 (C. C. A. 9th); *Vesper Co.* v. *Commissioner*, 131 F. 2d 200 (C. C. A. 8th); *Fox* v. *Harrison*, 145 F. 2d 521 (C. C. A. 7th). Section 115 (g) is not involved here, however.

one-half of the preferred stock may have been a step in a plan to substitute bank loans with a low rate of interest for B & K's obligations bearing a higher rate of interest, as the District Court found.[6] The existence of a plan, pursuant to which a cancellation and redemption of stock is made, has no special significance for purposes of Section 115 (i). Cf. *Hammans* v. *Commissioner,* 121 F. 2d 4 (C. C. A. 2d); *Irvine* v. *Commissioner,* 46 B. T. A. 246, 262. There is no suggestion here that there was a "reorganization" within the meaning of Section 112 (g) of the Revenue Act of 1936, which requires a plan as an incident thereof. As in *Malone* v. *Commissioner, supra,* p. 968, there was no reorganization but only a reduction of the corporation's capital. No conflict exists between the decision

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[6] Neither the stipulation itself (R. 23–28), the minutes of the meeting of the Board of Directors of B & K, held February 5, 1936 (R. 28–30), the stock redemption plan adopted at that meeting (R. 31–42), nor any of the other exhibits (R. 42–86) contains any statement that the stock redemption plan was linked with the payment of the gold notes in 1935. On the contrary, the stipulation shows that the plan for redemption of the preferred stock which was dated January 28, 1936 (R. 31), was not adopted by the directors of B & K until February 5, 1936 (R. 28), whereas the payment of the notes was completed in 1935, prior to either date. Thus, it would seem that the District Court's finding (R. 107) that the redemption of preferred stock was one step in a plan of refinancing to eliminate notes and preferred stock which bore high rates of interest and substitute therefor bank loans carrying a much lower rate of interest is also unsupported by any evidence.

of the lower court and the cases cited by taxpayer [7] (Pet. 5; Br. 26), since those cases all involved transactions in which a corporation was entirely liquidated as an incident of a statutory reorganization. Different considerations apply in such cases. Cf. *Commissioner* v. *Estate of Bedford,* 325 U. S. 283.

The rationale of cases such as *Gregory* v. *Helvering,* 293 U. S. 465, and *Pinellas Ice Co.* v. *Commissioner,* 287 U. S. 462, does not apply in this case. The definition of "amounts distributed in partial liquidation" for purposes of Section 115 is complete in itself, as has been seen. Furthermore, the stock redemption was in substance what it purported to be in form, since it had a corporate business purpose and was not undertaken solely for tax avoidance motives. Also, the corporation, having elected to use the form of a partial liquidation, as defined in Section 115 (i), is bound to accept the tax consequences thereof. Cf. *Higgins* v. *Smith,* 308 U. S. 473; *Moline Properties* v. *Commissioner,* 319 U. S. 436. Its stockholders can have no different rights with respect to the distribution than does the corporation.

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[7] *Commissioner* v. *Whitaker*, 101 F. 2d 640 (C. C. A. 1st); *Commissioner* v. *Kolb*, 100 F. 2d 920 (C. C. A. 9th); *Helvering* v. *Schoellkopf*, 100 F. 2d 415 (C. C. A. 2d); *Helvering* v. *Leary*, 93 F. 2d 826 (C. C. A. 4th); *Gutbro Holding Co.* v. *Commissioner*, 138 F. 2d 16 (C. C. A. 2d).

Since the distribution by B & K in 1936 was an amount distributed in partial liquidation as defined in Section 115 (i), the lower court correctly held that under Section 115 (c) of the Revenue Act of 1936 (Appendix, *infra*, pp. 24–25) all of the gain resulting to the taxpayer upon receipt of the distribution in redemption of part of his stock was includible in his income for 1936. The taxpayer's argument (Br. 22–23) that Section 115 (c) does not apply here because it is specifically limited to amounts distributed in partial liquidation "of a corporation", whereas Section 115 (i) deals with redemptions "of stock" is without merit. The definition of "amounts distributed in partial liquidation" in Section 115 (i) is stated to be a definition for the whole section (115). As a matter of fact, subsection (c) is the only part of Section 115 wherein the phrase "amounts distributed in partial liquidation" appears, other than in subsection (i) defining such term. It follows that the subsection (i) definition must have been designed to apply particularly to subsection (c). In no case of which we are aware, and taxpayer cites none, has it been held that Section 115 (c) does not apply to a distribution of a corporation which is an amount distributed in partial liquidation as defined in Section 115 (i). Instead, the two subsections have always been treated as related.

Finally, the view of the District Court (R. 99–102) that the legislative history of Section 115 (c) and (i) supports its theory that the gain on a distribution in partial liquidation was to be put on a capital gain basis and treated as a sale includible in income as provided in Section 117 (a) (Appendix, *infra*, pp. 25–26), instead of being included in its entirety in income as provided in Section 115 (c), was rejected in *Amelia H. Cohen Trust* v. *Commissioner,* 121 F. 2d 689, 691 (C. C. A. 3d). Accord: *Jones* v. *Commissioner,* 4 T. C. 854.

(2) In reversing the judgment of the District Court, the Circuit Court of Appeals did not abuse its power of review. The District Court erroneously thought that Section 115 (i) contemplated an intention to curtail or liquidate the corporate business, in addition to the express requirements stated therein (R. 90–102, 108), and it based its conclusion of law (R. 108) that the redemption of the preferred stock by B & K in 1936 did not amount to a distribution in partial liquidation within the statutory definition upon its erroneous understanding of what the statute contemplated. The Circuit Court of Appeals clearly had power to correct this erroneous interpretation of the controlling statute. This would be so even if the case

ad come from the Tax Court [8] (*Trust of Bingham . Commissioner*, 325 U. S. 365; *Dobson* v. *Commisioner*, 320 U. S. 489, 492–493, 502–503; *Security Iills Co.* v. *Commissioner*, 321 U. S. 281; cf. *Commissioner* v. *Heininger*, 320 U. S. 467; *Commissioner* v. *Wilcox*, decided by this Court February 25, 1946 (No. 163), and is certainly no less so where the appeal is from a judgment of the District Court. See *Merrill* v. *Fahs*, 24 U. S. 308, 310; *Dobson* v. *Commissioner*, *upra*, pp. 495, 498–499; *Kohnstamm* v. *Pedrick* (C. C. A. 2d), decided December 28, 1945 (1946 P–H, par. 72,324). Thus, it is unnecessary in this ase for the Court to decide whether the power of ppellate review is greater in an appeal from the District Court than in an appeal from the Tax

[8] The conclusion that a distribution is or is not one in partial liquidation within the first definition of Section 15 (i) has heretofore been treated as reviewable. See *Malone* v. *Commissioner*, 128 F. 2d 967 (C. C. A. 5th); *Alpers* . *Commissioner*, 126 F. 2d 58 (C. C. A. 2d); *Amelia H. Cohen Trust* v. *Commissioner*, 121 F. 2d 689 (C. C. A. 3d); *Kelly* v. *Commissioner*, 97 F. 2d 915 (C. C. A. 2d). But in any case such a question must be reviewable where, as here, he trier of the facts had an erroneous view of the statutory standard to be applied to the facts. Cf. *Trust of Bingham* . *Commissioner*, *supra*; *Malone* v. *Commissioner*, *supra*; *Kelly* v. *Commissioner*, *supra*.

Court.[9] In either type of appeal findings of fact by the trial court should be sustained on appeal, if supported by substantial evidence. But it does not follow that an appellate court is bound by a conclusion based on a misconception of the requirements of the controlling statute. Thus, *Blumenthal Print Works* v. *United States,* 141 F. 2d 211 (C. C. A. 5th), which holds only that a finding of the trial court supported by substantial evidence will not be overturned on appeal, is not in conflict with the decision below, as taxpayer asserts it is. (Pet. 4; Br. 19.)

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[9] Section 128 of the Judicial Code (Appendix, *infra*, pp. 27–28) gives a Circuit Court of Appeals broad jurisdiction to review by appeal final decisions of District Courts, but Rule 52 (a) of the Federal Rules of Civil Procedure (Appendix, *infra*, p. 28) states that findings of fact are not to be set aside unless clearly erroneous. On the other hand, a Circuit Court of Appeals may modify or reverse a decision of the Tax Court if it is not in accordance with law. Section 1141 (c) (1) of the Internal Revenue Code (Appendix, *infra*, p. 26). This Court has observed the distinction between the scope of review in the two types of appeal (*Dobson* v. *Commissioner*, *supra*, pp. 495, 497–499; cf. *Merrill* v. *Fahs*, *supra*, p. 310) and indeed seems to have accorded a broader appellate review in tax cases arising in the District Courts than in those coming from the Tax Court (cf. *Wisconsin Gas Co.* v. *United States*, 322 U. S. 526; *City Bank Co.* v. *McGowan*, 323 U. S. 594; *United States* v. *Seattle Bank*, 321 U. S. 583). See also *Kohnstamm* v. *Pedrick*, *supra*.

CONCLUSION

The judgment of the lower court is correct and is not in conflict with any decision, either on the merits or with respect to the scope of review. The petition for a writ of certiorari should therefore be denied.

Respectfully submitted.

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